

Notable Practice

Case Study - Medium Term Financial Strategy

Cambridge City Council

October 2008



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Executive summary

- 1 Cambridge City Council is a well-managed authority, rated as excellent by the Audit Commission in the 2003 Comprehensive Performance Assessment and with a current assessment of 'well above minimum standards' for use of resources.
- 2 The council initiated a 25-year medium term financial strategy in 1996 as a means to further improve its managerial capacity, when the council was already well managed. The MTFS is a comprehensive document of over 300 pages and is a tool to determine sustainable long-term spending plans, plan efficiency savings, finance invest-to-save projects from reserves, assess risks facing the council, plan its use of assets and rationalise its property portfolio. Members' confidence in the MTFS has been reflected in the setting of agreed target levels for Housing Revenue Account and General Fund reserves. The targets gradually reduce from £12m to about £2m in 2012, accompanied by effective plans to use funding above the target levels to improve services.
- 3 The construction of the MTFS is carried out with the involvement of members as well as officers across the council. The council's 'constitution' gives opposition parties rights to consult with officers and obtain financial information, but requires those parties to table their budget amendments in advance of the final budget-setting council meeting, so as to ensure they are fully costed and sustainable, using modelling based on the MTFS. The council has exceeded the Gershon targets in efficiency savings and has achieved balanced budgets each year since the adoption of the MTFS, through effective use of a cash limit system.

Local context

- 4 Cambridge City Council is a large district council, facing major pressures - particularly from population growth, demand for additional homes and pressure on available land for home-building.
- 5 The council strongly promotes environmental and financial sustainability. These policies have enabled the council to succeed in meeting strong demand for new homes on brownfield land. The council has entered into partnership arrangements with the county council and a neighbouring district council to provide further land for building in developments that span the city boundary.

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Background

- 6 Cambridge City Council is a well-managed authority, which has avoided crises. It has developed a strong and effective medium term financial strategy through evolution and good proactive management, not as a response to difficulties.
- 7 The germination of the council's MTFS (termed by the authority a Medium Term Strategy, or MTS, to reflect its wider role and content) preceded the adoption of a similar strategy by most other authorities and, indeed, prior to the recommendation by CIPFA of an MTFS, or the drawing-up of a template for an MTFS.

Strengthening financial management

- 8 On his appointment in 1996, the director of finance, David Horspool, evaluated the council's existing financial management practices and considered how to strengthen these. He concluded that a MTFS would assist the council in making longer-term and more sustainable decisions, as well as better integrating service and financial planning. Objectives for the MTFS included integrating all aspects of the council's planning into a single document.
- 9 Horspool's proposal to establish the MTFS was greeted favourably by the chief executive, other senior officers and members, because all could see the benefits offered by it. The MTFS produced information that was useful to them and which they could see enhanced their ability to fulfil their roles.
- 10 Horspool says that his previous work experience - he was previously deputy treasurer at another district council - suggested that a comprehensive MTFS was necessary for any authority to have effective and sustainable medium term financial planning and management. It was clear to him that this was what he terms 'a sensible approach'.
- 11 The first MTFS was produced for the financial year 1997/98, taking a co-ordinated view of the council's finances. It brought together information on the General Fund, the Housing Revenue Account (HRA), capital and revenue expenditure plans and forward projections on predicted and required revenue, capital receipts, service costs and potential savings from service efficiencies.
- 12 Initially, the MTFS was a relatively short document of a few dozen pages. Subsequently, the MTFS grew as new information sources and analysis were added and now contains over 300 pages, including an executive summary, itself of about 30 pages. As the council - its members and officers - increasingly demanded the ability to forward plan effectively, so the MTFS has become more comprehensive.
- 13 By bringing together service plans and council priorities, the MTFS enables members to allocate resources in accordance with policy priorities. It also links with a risk database and an analysis of the uncertainties affecting the council, so that potential liabilities and other threats to financial projections are taken into consideration when

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service and financial decisions are taken. The risk database considers corporate, service and project risks. A summary of the highest rated risks is incorporated in the MTFS as context for financial decisions, in particular setting target levels for reserves. The MTFS itself is also fully risk-assessed.

- 14 Despite its length, the MTFS remains a 'high level' document, containing minimal detail. It is supplied to all members and has proved useful to councillors, as well as officers, for planning and reference purposes.
- 15 Prior to the adoption of an MTFS, Cambridge had a financial planning system that was typical for a district council - each service department reported to committee and a summary of the agreed resource allocations to departments was brought together as a budget document for consideration in the council's annual budget-making meeting. Forward projections were limited to the following two years. Through the MTFS, the council brought together all of its core financial and service management information into one document, "making sense of the inter-relationships," as Horspool puts it.
- 16 Alongside the MTFS, the council introduced cash limits for each service, to provide assurance on delivery of the overall control totals. This has worked exceptionally well, delivering balanced budgets in every year since the system was adopted. It has assisted the council to implement efficiency savings which have exceeded - and in many cases pre-dated - the Gershon savings targets.

The council constitution

- 17 Financial sustainability is reinforced by Cambridge City Council's constitution. A detailed budget-setting programme has been agreed with the majority and opposition groups (there were formerly two opposition groups that endorsed the programme, though there is now only one opposition group on the council). This gives an opposition party full access to officers in drawing-up alternative budget proposals. In return, the proposals must be set against the context of the council's existing financial plans. All budget proposals must be formally submitted to committee in advance of the annual budget-making full council meeting. This prevents uncosted and unrealistic budget proposals being tabled at the last minute and ensures that opposition budget proposals are themselves financially sustainable.
- 18 The MTFS provides officers with the capacity to demonstrate to members why capital receipts need to be spent in a planned way, showing how today's receipts may be necessary to meet known demands in future years that would otherwise be unaffordable. This approach underpins the council's policy of financial sustainability.

Asset management

- 19 In recent years, the remit of the MTFs has gradually been extended effectively, including using it to improve asset management. All major assets are now reviewed through the council's Property Portfolio Review, which operates in conjunction with the MTFs. The review uses objective data to consider the value and contribution of existing assets. Methods to assess the value of commercial property include the return on capital employed, which has led to the identification of under-performing assets and their subsequent disposal. Assets that are not used for commercial purposes are assessed on the basis of alternative uses, and how their existing use assists the council to meet broader policy objectives.
- 20 Possible disposals are considered in the first instance by the Asset Management Group - an officer group, which provides a corporate overview. Recommendations of the Asset Management Group go to the Corporate Management Team and, if endorsed, on to the relevant service committees for final decision.
- 21 Options for disposal are evaluated, ranging from maximising capital receipts to making land available for social purposes – in return for lower capital receipts - for example, for developments that include affordable housing or have a reduced carbon footprint. The council's systematic review of its property portfolio has assisted with its objective of ensuring that a high proportion of new home building is on brownfield land and as a result it has actually exceeded its own target - an achievement commended by the Audit Commission.
- 22 In some instances, there is a conflict between the commercial and policy objectives. For example, car parks produce a high rate of capital return, but contravene the policy objectives of the city and county councils of reducing traffic congestion and city centre car use. In these circumstances, the availability of comprehensive information allows a balanced strategy to be adopted; in this instance through the local traffic management plan.
- 23 To create a co-ordinated approach to resource management, responsibility for the property portfolio was transferred to the finance department in 2007. The identification of under-performing assets, and taking action to improve their use, is a priority objective for the council. This has led to millions of pounds of capital receipts being made available for re-investment, and a reduction in asset maintenance costs.

Managing reserves and investments

- 24 The MTFs is used to actively manage the level of reserves for both the HRA and General Fund. This is demonstrated in the current plans to reduce the level of General Fund reserves from £12m to the target level of £5m by 2015. Reserves are drawn on to provide temporary initial financing for invest-to-save schemes, with members given assurance on the reliability of savings and the sustainability of reserves by the long-term forward financial projections.

Asset management

- 25 By having extensive forward projections - the MTFS covers a 25-year period - members can see that savings from investments can be justified by taking a long-term perspective. This is particularly important for the council given its use of reserves to finance invest-to-save projects. The longer-term perspective gives members the assurance they need that they can authorise the medium term reduction in reserve levels as they can see that these are projected to rise again subsequently. This has been demonstrated in the case of the current investment in customer access improvements.
- 26 The 25-year financial model underpins Cambridge's version of the MTFS, and includes its projection of council tax rises in years going forward. By demonstrating that the budget balances over a forward period, members can see that their financial proposals are sustainable. Moreover, councillors are effectively prevented, by the forward-modelling, from putting forward short-term and electorally attractive lower council tax increases that are financially unsustainable when projected forward. The current MTFS assumes an annual council tax increase of 4.5 per cent for the next four years.

Service planning

- 27** One of the principles of the MTFS is that it is decisions on service priorities that must determine finance, rather than the other way round. Accordingly, the service plans are brought together within the MTFS in the annual planning and decision-making cycle. These service plans can produce resource amendments - bids for growth, or planned reductions in expenditure, reflecting efficiency gains or other savings.
- 28** As part of the annual budget-making process there is an annual review of current service plans each November, which identifies any potential resource amendments. The reviews take into account local and national performance indicators and benchmarking against comparable authorities, where available.
- 29** However, the Audit Commission had previously commented that while Cambridge's MTFS process is excellent, its performance management is comparatively weak. The authority accepts that while performance management has been strengthened in recent years, it still needs further improvement.
- 30** All major contracts are listed within the MTFS, including the renewal date, to provide indication of the timings of potential step-changes in related costs.

A 25-year strategy

- 31 The Government specifies a 30-year model for the Housing Revenue Account. If this is appropriate for the HRA, the council believes it makes sense for a similar timeframe to be used for the general fund and capital spending. Further, if there is to be effective integration of all the council's finances, then there needs to be a similar timeframe for all the budgets.
- 32 The council believes that a 25-year period is a timeframe that demonstrates genuine sustainability. A shorter period would lose some of the benefits that can be achieved by forward financial planning: for example, a five-year perspective would not justify the use of reserves to fund many invest-to-save projects. An example is with the financing of mercury abatement works required at the crematorium.
- 33 The use of the MTFS has helped plan efficiency savings over a sustained period - it has not been necessary to generate more savings to meet the government's 3 per cent efficiency savings targets. The Audit Commission has commended the council for its success in generating Gershon savings - it met the Gershon three-year targets within two years.
- 34 A longer-term strategy is particularly important for the council because of the projected growth in dwellings and population. While there is some short-term growth, the major impacts will be from 2011 - so it is important for the council to have assurance that it has the resources and policies that are appropriate for the challenges associated with that growth.
- 35 The strategy also helps inform the council in undertaking its section 106 negotiations, so that, in particular, the council is aware of the medium and longer-term implications on the revenue budget of any additional capital assets that are provided under section 106 arrangements.
- 36 The 25-year strategy also helps to provide the context for the council's policy on asset disposals. By having that longer-term outlook, the council can decide on disposals while considering its longer-term need for land and buildings in delivering effective services.

How has the strategy been tested?

- 37 The MTFS has helped improve the management of the council's reserves. Members have confidence in the 25-year strategy, which has enabled them to approve the use of reserves to finance invest-to-save schemes.
- 38 The director of finance's section 25 reporting has been made easier by the comprehensive character of the MTFS. One of the benefits of the detail of the MTFS is that it provides detailed and comprehensive assurance in relation to:
- the robustness of the estimates used for calculating the budget; and
 - the adequacy of the proposed financial reserves.
- 39 A higher than predicted pay settlement agreed by local government employers provided a last minute challenge for the council in its September 2007 MTFS. This caused the council to increase its requirement for efficiency savings to maintain its financial strategy.
- 40 The MTFS proved important in assisting the council in delivering a well-managed transfer of political leadership, when the council moved from a long period of Labour control, to outright Liberal Democrat control in May 2000. The change in political leadership led to major changes in spending priorities – resulting in over £300,000 of revenue changes and £345,000 in capital spending (as well as £400,000 per annum for the next three years) - but the process was conducted in an efficient and effective manner.
- 41 Initial adoption of the MTFS was so long ago that there is no clear recollection of the challenges involved in implementation - which probably means that there were no significant challenges.

Learning and outcomes

42 The external auditors through most of this period were PricewaterhouseCoopers. Both PwC and the Audit Commission were fully informed throughout of the MTFS and its evolution and were fully supportive, though they did not play an active role in its adoption.

Lessons learnt

- Cambridge would not advise another authority to merely copy its approach - rather a council should adopt systems that best suit its own circumstances. It should do what works for it.
- The objective should not necessarily be a 300 page MTFS, but an MTFS that meets a council's needs. A comprehensive MTFS will often best be achieved by evolution, not instantly. An attempt to produce a comprehensive document very quickly is likely to create an unbearable burden on many authorities - especially district councils with limited staffing resources.
- It is hard to obtain sufficient resources at a district council to support the move to an MTFS all in one go. Outcomes need to be balanced against the resources needed to achieve them.
- Achievability must be over a number of years, with each stage manageable. It is not sensible or effective to move too quickly to an over-ambitious or comprehensive MTFS.
- There needs to be a realistic timetable during the year for the stages which come together for an MTFS. It is important to make it easy for service heads to contribute to the MTFS and not to make last minute demands for information from them, particularly at times of the year when they have other onerous obligations.
- It is best to ask service heads for information at a time of the year when their other demands are lower and to only seek information that they would need to provide anyway. In this way, the MTFS can assist service heads' work management, rather than be an additional demand on them.
- Only collect the information that is necessary.
- Get the close involvement and 'ownership' of the corporate management team for the MTFS process.
- Involve members from both the ruling and opposition groups. Get cross-party support for the strategy. Work closely with the opposition as well as the ruling group. This can ensure that the approach will survive any change in political control.
- The MTFS can co-ordinate the council's service management and policy prioritisation process. This can demonstrate to staff why activities are important: for example, why risk assessment is important and justifies the time necessary to make it reliable.

Outcomes

- The Audit Commission has assessed Cambridge as an 'excellent' authority in its CPA and CA reports.
- Cambridge has been assessed as 'excellent' in its use of resources, enabling it to balance its budget in a challenging environment, says the Audit Commission.
- Every year in which it has used the MTFs, the council has achieved balanced budgets without the need to identify additional savings during the financial year.
- The council has been effective in identifying and achieving efficiency savings, a process begun before the Gershon targets were set and exceeding the Gershon targets.
- Cash limits have worked.
- The use of the council's Policy Priority Fund, creating 'policy space' to enable effective redirection of resources, has been effective in enabling the council to respond to policy changes.
- Capital receipts from asset disposals have been worth several million pounds and assisted the council to meet broader policy objectives. The MTFs has helped the council to identify assets that are disproportionately costly to maintain or make insufficient contribution to policy aims, encouraging them to dispose of these and reduce asset maintenance costs.
- The asset disposal policy has helped the council to exceed its targets in building new homes on brownfield land.

Sources:

- Meeting with David Horspool, director of finance, Cambridge City Council
- Cambridge City Council's Medium Term Strategy
- Audit Commission, Corporate Assessment
- Audit Commission, Comprehensive Performance Assessment
- Audit Commission, Annual Audit Letter

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For further information on the work of the Commission please contact:

Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ

Tel: 020 7828 1212 Fax: 020 7976 6187 Textphone (minicom): 020 7630 0421

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